

**Statement**  
**of**  
**Timothy J. McCormally,**  
**Executive Director**  
**on behalf of**  
**Tax Executives Institute, Inc.**  
**before the**  
**IRS Oversight Board**  
**March 7, 2007**

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Good morning. I am Timothy J. McCormally, Executive Director of Tax Executives Institute, and I am accompanied today by Eli J. Dicker, the Institute's Chief Tax Counsel. We are pleased to participate in today's meeting of the IRS Oversight Board on the tax gap.

**Background**

Tax Executives Institute is the preeminent global association of corporate tax executives. Our more than 6,800 members are accountants, attorneys, and other business professionals who are employed by approximately 2,800 of the leading companies in the United States, Canada, Europe, and Asia. TEI represents a cross-section of the business community, and is dedicated to the development and implementation of sound tax policy and to promoting the uniform and equitable enforcement of the tax laws. The Institute is proud of its record of working with congressional committees, government agencies (including the Internal Revenue Service, Department of the Treasury, and the Securities and Exchange Commission), and other policy-making bodies (such as the Financial Accounting Standard Board and the Public Company Accounting Oversight Board) to

minimize the cost and burden of tax administration and compliance to the mutual benefit of the government, business, and ultimately the public.

TEI members are responsible for conducting the tax affairs of their companies and ensuring their compliance with the tax laws. Thus, members deal with the tax code in all its complexity, as well as with the IRS and other tax administrators, on a daily basis. Indeed, the bulk of TEI's members work for companies that are part of the IRS's Coordinated Industry Cases program, pursuant to which they are subject to continual examination. TEI is proud that the companies for whom our members work have perhaps the highest compliance rate of any single group of taxpayers. We are also proud of the Institute's record of working with the IRS to facilitate the agency's corporate e-filing mandate, its design and rollout of Schedule M-3, and a plethora of other initiatives to enhance tax administration and improve compliance.

## **Discussion**

### **I**

TEI applauds the Oversight Board's decision to focus this year's public forum on the tax gap. In its meeting notice, the Board observed that —

[r]educing the tax gap is not just the responsibility of the IRS, but of all organizations that are engaged in tax administration. The tax gap affects us all as taxpayers and citizens, and we cannot expect the IRS to bear the burden of reducing the tax gap on its own.

Few would dispute that all taxpayers, associations, and other stakeholders — public or private, individual or corporate — have a stake in closing the tax gap and a duty to do what they can to do so. The collective efforts of us all should, over time, enhance tax compliance, increase government revenues, and optimally build taxpayer confidence that more if not most taxpayers are paying their fair share of tax.

That said, we believe it is necessary to acknowledge at the outset that the government has already conscripted employers and the business community generally

into the service of tax administration, requiring them to withhold and file Forms W-2 and 1099, as well as other information returns — all without providing compensation for what, in the government sector, would be called an unfunded mandate. It is also important to acknowledge that, while the IRS cannot be expected to do it all, the call for a balanced, shared approach to dealing with the tax gap must constitute more than the shift of responsibility for improving compliance from the government to the private sector. To be sure, the United States cannot “audit its way out of the tax gap,” but in TEI’s view the IRS must be held accountable for accurately measuring the tax gap and implementing strategies to reduce it.

Congress, in turn, must be held responsible for properly funding the IRS. Hyperventilating about the tax gap is a poor substitute for an effective, adequately staffed tax compliance strategy. Nor is it, in our view, a valid basis for sidestepping the overriding issue of tax simplification. Indeed, as the Oversight Board has noted, a significant portion of the tax gap is attributable to the Internal Revenue Code’s mind-numbing complexity.

## II

Pragmatically addressing the tax gap requires three things accomplished sequentially — a common definition; accurate and up-to-date quantification; and balanced remedial measures.

As for the definitional challenge, the very term “tax gap” seems to take on a different form and shape depending on who is talking about it. It is generally agreed that the “tax gap” is a measure of noncompliance, the difference between the amount of tax owed and the amount of tax paid (voluntarily). But that is not how the term is universally used. For some, the term “tax gap” is used expansively, if not recklessly, to encompass not only what is currently owed but that which the definer believes should be owed; for these individuals, the tax gap is measured not against the tax system we have, but rather the tax system they wished we had.

Closely related to definition is measurement. How large *is* the tax gap? Obviously, it depends on what the meaning of the term is. But it also depends on the collection and analysis of compliance data that can be tested and retested over time. One of the curious aspects of the current tax gap focus is the absence of hard evidence documenting that the problem is any larger, or for the matter smaller, than in the past. Based on the available data, the compliance rate appears to be between 80 and 85 percent — just about what it was 10 years ago and 20 years ago.

TEI certainly does not believe a noncompliance rate of 15 to 20 percent is acceptable or should be tolerated. Indeed, the data suggest that corporations generally — and large corporations in particular — have extraordinarily high compliance rates. This is not only because they are subject to ongoing audit by the IRS, but because of their internal controls (made stronger by the Sarbanes-Oxley Act), the salutary role of independent public auditors, and (in respect of publicly held companies for which earnings reports loom large) the general incentive *not* to underreport income. It is also due, we believe, to the professionalism of the internal and external tax advisers employed by corporate taxpayers.

We do believe, however, that taking precipitous action based on dated projections and estimates is a recipe not for success but for finding ourselves in precisely the same situation in another decade. Ready, fire, aim is not the way to proceed.

### III

Finally, let me offer a few observations about the data that is currently available and extant proposals to address the gap.

First, as previously suggested, the data suggest that the largest part of the tax gap problem originates in the individual and small business segments of taxpayers. The Treasury Department, for example, cites data suggesting that more than 90 percent of the gross tax gap is attributable to these sources. Assuming the validity of this data, the IRS needs to focus on noncompliant taxpayers, developing a multi-year strategy that employs

a mixture of tools: technological innovation, administrative and regulatory guidelines, and traditional compliance activities.

Second, proposals to expand information reporting requirements (*e.g.*, payments to corporate payees) would impose significant costs on the payer community — payers that, by all accounts, are themselves compliant. While there may be no substitute for securing the information from the payer community, collection costs should be weighed (in terms of dollars, time, and the degree of intrusion) against the dollars to be collected. What is more, consideration should be given to compensating the payer community for the additional burdens incurred in assuming a greater role in the tax administration system. We note, for example, that many states provide a so-called vendor allowance to merchants to partially offset their costs in collecting and remitting sales tax.

Finally, before imposing additional burdens on the business community, the IRS should be able to demonstrate its ability to use effectively the information it already receives and, by extension, the additional information that will come its way. To impose additional reporting requirement and force companies to update their information systems without assessing the IRS's short-term ability to use the newly reported information would not only be wasteful but could undermine confidence in the tax system.

## **Conclusion**

Tax Executives Institute again commends the IRS Oversight Board for holding this public forum on the tax gap. TEI looks forward to working with the Oversight Board, the IRS, Treasury, and others who have a stake in addressing this important challenge. TEI members bring unparalleled experience to tax and business decision making, and the Institute stands ready to participate in efforts to improve our tax administration system and specifically to develop effective approaches to addressing the tax gap.